THUERINGISCHE FASER AKTIENGESELLSCHAFT SCHWARZA

v.

BANK OF COMMERCE (M) BHD

HIGH COURT MALAYA, KUALA LUMPUR
T SELVENTHIRANATHAN J
[SUIT NO: D7(D1)-22-96-1996]
28 NOVEMBER 2008

BANKING: *Banker and customer - Fixed deposit - Bank withholding repayment to plaintiff of monies in plaintiff's fixed deposit account - Whether there was agreement between plaintiff and bank that monies in account were security for alleged comfort agreement between plaintiff's holding company and bank*

COMPANY LAW: *Separate legal entity - Holding and subsidiary companies - Principles applicable*

BANKING: *Banker and customer - Fixed deposit - Conversion of monies in fixed deposit account to foreign currency with retrospective effect - Whether ought not to be allowed*

The plaintiff, a company established in Germany, instituted this action against the defendant ('bank') as a result of the latter's refusal to pay over to the plaintiff monies that had been placed on interest-bearing fixed deposits with the bank by the plaintiff. Around 1992, the plaintiff had opened a fixed-deposit account with the bank and remitted a total sum of DM9,000,000 (converted at that time to RM15,117,528.50) to be placed on fixed-deposit with the bank at a tenure of three months with a roll-over on the same tenure at the bank's prevailing interest rates. The bank issued fixed-deposit receipts for the same in the plaintiff's name, and the only authorised signatories in respect of the fixed-deposit account were two German nationals named Gunther Schmidt ('PW2') and Hartmut Krannich ('PW3') respectively, who were to act jointly. The plaintiff became a subsidiary of a company incorporated in Malaysia called Twenty First Century Oils Sdn Bhd ('TFCO') and placed the monies in question on fixed deposit with the bank upon the representation of TFCO that the interest rates offered by the bank at the material time were more attractive than the interest rates available

in Germany then. The plaintiff was not aware when so doing that the bank had loaned monies in the region of RM30,000,000 to TFCO and the latter had passed a resolution to the effect that the monies placed on fixed deposit by the plaintiff with the bank were to remain with the bank as "comfort" or as an assurance to the bank for the repayment of the loan granted to TFCO. The plaintiff was at all material times totally unaware of such a resolution having been passed by TFCO and communicated to the bank; neither did the bank inform the plaintiff of the resolution. It was only after the plaintiff initiated investigations into the banks refusal to make repayment was it revealed that the bank was relying on the "letter of comfort" issued by TFCO based on TFCO's resolution to withhold repayment of the monies in the plaintiff's fixed-deposit account. The plaintiff also filed an application in encl. 49 to amend the reliefs sought by converting the RM15,117,528.50 in fixed deposits with the bank together with accrued interest thereon back into Deutsche Marks at the then prevailing exchange rates and then to further convert the amount from Deutsche Marks to Euro Dollars.

Held (allowing the plaintiff's claim for refund of its fixed deposits; dismissing the plaintiff's application in encl. 49):

(1) The bank had failed to produce any evidence to contradict the plaintiff's position that there was no understanding or agreement between the plaintiff and the bank whereby the monies placed in its fixed-deposit account were to be treated as security for the alleged comfort agreement between TFCO and the bank. PW2 and PW3 were the only two authorised signatories of the plaintiff's fixed-deposit account with the bank, and they did not assign or relinquish their rights to operate the account to anybody else. Thus, the bank had breached its duty as a banker in unilaterally setting-off the monies in the plaintiff's fixed-deposit account against the monies owed to the bank in the delinquent account of a third party, namely TFCO, without even enquiring as to whether the plaintiff agreed or consented to such action by the bank. While it was not disputed that TFCO was the sole shareholder of the plaintiff when the fixed deposits were placed with the bank, the fact remained that it was the plaintiff which placed the fixed deposits with the bank and not TFCO, a separate legal entity from the plaintiff. It is trite law

that the parent or holding and subsidiary companies are separate legal entities in company law and a board resolution of one company, even if is the parent or holding company, cannot bind a subsidiary or wholly-owned company of that parent or holding company. No evidence was adduced by the bank to show that the plaintiff had consented to TFCO using the plaintiff's fixed deposits as "security comfort" for the banking facilities granted by the bank to TFCO. At best, the alleged "comfort arrangement" was on a mutual faith basis between TFCO and the bank only, as the plaintiff was never a party thereto. Further, if the fixed deposits were to be secured against TFCO's indebtedness, then there should have been compliance with s. 108 of the Companies Act 1965. There was absolutely no compliance with this provision of law and, hence, the bank as the alleged chargee of the fixed deposits had no right over the alleged security which would "be void against the liquidator and any creditor of the company". At the conclusion of all submissions, the bank had failed to raise any credible defence to the plaintiff's claim for the refund of its fixed deposits together with the accrued interest thereon. (paras 11, 12, 18, 20, 21 & 26)

(2) In respect of the plaintiff's application in encl. 49, since the plaintiff had made a business decision to place its monies on fixed deposit in Ringgit Malaysia with the bank in Malaysia, it should not be allowed to convert the monies to Deutsche Marks and Euros with retrospective effect to its advantage. It had to bear the risk that was attendant upon its business decision. As the plaintiff chose to invest in Malaysia, it had to abide by the economic regime in Malaysia. It would, of course, on realisation of the judgment sum be at liberty to convert the same into any currency of its choice at the prevailing rate of conversion to repatriate the monies out of Malaysia. (para 27)

Legislation referred to:
Companies Act 1965, s. 108
Evidence Act 1950, s. 114(g)

Federal Stock Corporation Act [Germany], s. 111

For the plaintiff - Andrew Ng Ko Chee (Izawati Wook with him); M/s Yeo & Yeo
For the defendant - Ramesh Sathasivam; M/s Adnan Sundra & Low

Reported by Suresh Nathan

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JUDGMENT

T Selventhiranathan J:

[1] The plaintiff, a company established in Germany, instituted this action against the defendant bank ("the bank") as a result of the latter's refusal to pay over to the plaintiff monies which had been placed on interest-bearing fixed deposits with the bank by the plaintiff.

[2] A bankruptcy order (equivalent to a winding-up order under the company of law of Malaysia) was made against the plaintiff on 31 August 1993 by the District Court of Gera in Germany and one Dr Winfrid Andres, PW1, was appointed the trustee in bankruptcy of the plaintiff (equivalent to a liquidator under the company law of Malaysia) and was duly authorized to administer the assets of the plaintiff. He instituted this action on behalf of the plaintiff in such capacity.

[3] There was uncontroverted evidence that around 1992 the plaintiff opened a fixed-deposit account with the bank and remitted a total sum of DM9,000,000 (converted at that time to RM15,117,528.50) to be placed on fixed-deposit with the bank at a tenure of three months with a roll-over on the same tenure at the bank's prevailing interest rates. The bank issued fixed-deposit receipts for the same in the name of the plaintiff. The only authorized signatories in respect of the said fixed-deposit account were two persons by the names of Gunther Schmidt and Hartmut Krannich, who were to act jointly. They are both German nationals and were called and testified at the trial as PW2 and PW3 respectively.

[4] Evidence was led to the effect that the plaintiff became a subsidiary of a Malaysia-incorporated company called Twenty First Century Oils Sdn Bhd ("TFCO") and that the plaintiff placed the monies in question on fixed deposit with the bank upon the representation of TFCO that the interest rates offered by the bank at the material time were more attractive than the interest rates available in Germany then.

[5] The plaintiff was not aware when so doing that the bank had loaned monies in the region of RM30,000,000 to TFCO and the latter had passed a resolution to the effect that the monies placed on fixed deposit by the plaintiff with the bank were to remain with the bank as "comfort" or as an assurance to the bank for the repayment of the loan granted to TFCO.

[6] The plaintiff was at all material times totally unaware of such a resolution having been passed by TFCO and having been communicated to the bank. Neither did the bank inform the plaintiff of such a resolution having been passed.

[7] Even when the German solicitors of the plaintiff wrote to the bank by letter dated 25 June 1993 demanding the repayment of all monies together with interest in the fixed-deposit account of the plaintiff, the bank refused to make any repayment and further did not condescend to assign any reason for such refusal. It was only after the plaintiff initiated investigations into the bank's refusal to make the repayment was it revealed that the bank was relying on the "letter of comfort" issued by TFCO based on the abovementioned resolution of TFCO to withhold repayment of the monies in the plaintiff's fixed-deposit account.

[8] It cannot be gainsaid that at all material times the plaintiff was never aware of the existence of the said "letter of comfort" nor of any arrangement made between the bank and TFCO leading to the issuance of the said "letter of comfort". As the plaintiff was never a party to nor had prior knowledge of its issuance, the bank could not rely on it to deny the plaintiff's rightful entitlement to the monies in its fixed-deposit account. On the other hand, the fact that the bank dragged its feet in revealing to the plaintiff the reasons for its refusal to honour its contract with the plaintiff in relation to the monies placed on fixed deposit could not but raise doubts in the mind of the court as to the propriety of the conduct of the bank. At all material times the plaintiff had a clear understanding with the bank that the account it opened was solely and strictly for the operation of a fixed-deposit account to earn interest at what the plaintiff considered to be attractive rates.

[9] The bank's case was that the fixed deposit placed by the plaintiff was security comfort for the facilities granted to TFCO by the bank in light of the fact that TFCO was the holding company and the sole shareholder of the plaintiff at the material time and that the plaintiff was aware that the fixed deposit was placed for such purpose.

[10] However, the testimony of the plaintiff's witnesses, which I accepted as true, demolished the bank's argument. If indeed the plaintiff was aware of the arrangement relating to the security comfort to be provided by the plaintiff as contended by the bank, then the bank should logically have revealed such arrangement with alacrity to the plaintiff at the first opportunity that arose. This the bank did not do and its motive in withholding this information from the plaintiff until it was forced to reveal it effectively destroyed the bank's case.

[11] At the conclusion of the trial, I found that the bank had failed to produce any evidence to contradict the plaintiff's position that there was no understanding or agreement between the plaintiff and the bank whereby the monies placed by the plaintiff in its fixed-deposit account were to be treated as security for the alleged comfort arrangement between TFCO and the bank.

[12] It was my finding of fact that Gunther Schmidt (PW2) and Hartmut Krannich (PW3) were the only two authorized signatories of the plaintiff's fixed-deposit account with the bank and that they did not assign or relinquish their rights to operate the account to anybody else. Thus the bank breached its duty as a banker in unilaterally setting-off the monies in the plaintiff's fixed-deposit account against the monies owed to the bank in the delinquent account of a third party, namely TFCO, without even enquiring as to whether the plaintiff agreed or consented to such action by the bank.

[13] My findings upon scrutinizing the evidence of the witnesses and the exhibits tendered during the trial were as follows.

[14] The bank failed to produced any evidence during the trial to contradict the plaintiff's claim that no agreement was entered into between the plaintiff and the bank whereby the plaintiff's fixed deposits were placed as security for the alleged "comfort arrangement" between TFCO and the bank.

[15] The plaintiff was an entity incorporated in Germany and was governed by the Federal Stock Corporation Act of Germany. There were two statutory bodies running the plaintiff, namely, the management/executive board and the supervisory board. The management/executive board was responsible for the day-to-day running of the plaintiff and to represent the plaintiff in entering into binding contracts. The status of the management/executive board could be likened to that of the board of directors of a company incorporated in Malaysia. The supervisory board, on the other hand, consisted of members appointed in a general meeting, usually by the shareholders and employee representatives. The supervisory board's duties were provided in s. 111 of the Federal Stock Corporation Act of Germany where it was to supervise the management of the plaintiff but was not to engage in the management duties of the plaintiff. Therefore, the supervisory board and its members had no legal capacity to bind the plaintiff through their acts or conduct.

[16] In the present case, PW2 and PW3 were at all material times the only two members of the management/executive board representing the plaintiff and they were also the only two signatories authorized by the plaintiff in opening the fixed-deposit account with the bank as evidenced in exh. "P9" at p. 12 of bundle B of the bundles of documents tendered in evidence.

[17] DW1, the bank's first witness, also testified in cross-examination that PW2 and PW3 were the two authorized signatories of the plaintiff's fixed-deposit account with the bank and that they did not assign their rights to operate the account to anybody else. In the circumstances I found that only PW2 and PW3 could deal with the fixed-deposit account of the plaintiff to the exclusion of all others, including any member of the supervisory board of the plaintiff unless there was a fresh mandate issued by the plaintiff to the bank to say otherwise. There was no evidence of such a fresh mandate whatsoever. Thus, the bank breached its duty of care as a banker in unilaterally setting-off the plaintiff's fixed deposits against a third party's, ie, TFCO's, delinquent account without so much as enquiring from the plaintiff as to its consent or agreement to such set-off.

[18] While it was not disputed that TFCO was the sole shareholder of the plaintiff when the fixed deposits were placed with the bank, the fact remained that it was the plaintiff which

placed the fixed deposits with the bank and not TFCO, a separate legal entity from the plaintiff. It is trite law that the parent or holding and subsidiary companies are separate legal entities in company law and a board resolution of one company, even if it is the parent or holding company, cannot bind a subsidiary or wholly-owned company of that parent or holding company.

[19] Following thereon, even if a director of TFCO had sat on the supervisory board of the plaintiff, it could not be said that he was wearing the hat of TFCO when so sitting, and hence any imputed knowledge that he may have had of the alleged "comfort arrangement" between TFCO and the bank should have passed on to the plaintiff. This was because, firstly, there was no evidence whatsoever that the plaintiff through its management/executive board was privy to the said "comfort arrangement" and, secondly, the only link between TFCO and the plaintiff *vis-à-vis* the fixed deposits were the two agreements marked as exhs. "P11" and "P12" which reinforced the testimonies of PW2 and PW3 that the placing of the fixed deposits with the bank was for the sole purpose of earning a higher rate of interest than could have been obtained in Germany.

[20] The circular resolution dated 28 August 1992 and introduced by DW2 as exh. "D18" at pp. 40 to 41 of bundle B of the bundle of documents produced in court was therefore inconsequential and void as against the plaintiff as the plaintiff had no knowledge of it whatsoever, leave alone having consented to it. No evidence was adduced by the bank to show that the plaintiff had consented to TFCO using its (the plaintiff's) fixed deposits as "security comfort" for the banking facilities granted by the bank to TFCO. At best, the alleged "comfort arrangement" was on a best mutual faith basis between TFCO and the bank only, as the plaintiff was never a party thereto.

[21] Further, if indeed the fixed deposits were to be secured against TFCO's indebtedness, then there should have been compliance with s. 108 of the Companies Act 1965. DW1 in cross-examination testified that there was absolutely no compliance with this provision of the law and hence the bank as the alleged chargee of the fixed deposits had no right over the alleged security which would "be void against the liquidator and any creditor of the company".

[22] The bank also raised the issue of whether the corporate veil should be lifted against the plaintiff on the basis that the plaintiff was a subsidiary of TFCO. One of the essential elements which has guided the courts in piercing the corporate veil is when fraud is found against the companies involved. However, in the present case, no allegation of fraud at all was canvassed by the bank nor was there any evidence raised to link any fraudulent or collusive attempt by both companies, ie the plaintiff and TFCO, to defraud the bank. Whilst the plaintiff may well be the subsidiary of TFCO, TFCO did not run the plaintiff nor have management control over it. As adverted to earlier, the plaintiff was run by its management/ executive board which consisted of PW2 and PW3 who were independent of the plaintiff's shareholder TFCO. In the circumstances there was no basis for this argument of the bank that there was a corporate veil in place between the plaintiff and TFCO which should be lifted.

[23] There was also no justification or basis for the bank to cast aspersions on the testimony of the plaintiff's witnesses as I found them to be truthful and credible. Learned counsel for the bank wanted records of the plaintiff produced during the trial although there had been no pre-trial application for discovery. In this regard, PW1 testified that all records and documents generally were only required to be kept for up to a period of ten years under German law, which period had since lapsed in the present case and the person who would had custody of the same would have had them destroyed as was the usual practice. I accepted this testimony as fact as no evidence was adduced on behalf of the bank to show that this was not the case. Furthermore, the bank had had ample time from the filing of the action in 1996 to have applied for discovery. But it did nothing until midway in the trial.

[24] Moreover, PW1 was a court-appointed liquidator who impressed me in the witness box with his testimony and I had no reason to doubt him when learned counsel for the bank unfairly put it to him without evidence to back up the suggestion that he was lying and that the records were still available. It must also be appreciated that throughout the life of this case for close to ten years nothing was requested by the bank in relation to the documents which were being sought so late in the day. There was no question therefore of the plaintiff refusing to comply with a

reasonable request. As such the presumption of making an adverse inference under s. 114(g) of the Evidence Act 1950, which the bank wanted the court to draw, could not be invoked here where there has been no withholding or suppression of evidence on the part of the plaintiff.

[25] After the testimony of all the witnesses had been adduced, the plaintiff filed an application in encl. (49) to amend the reliefs sought by converting the RM15,117,528.50 in fixed deposits with the bank together with accrued interest thereon back into Deutsche Marks (DM) at the then prevailing exchange rates and then to further convert the amount from DM to Euro Dollars ("Euros"). This application was strongly resisted by the bank.

[26] At the conclusion of all submissions, I found that the bank had failed to raise any credible defence to the plaintiff's claim for the refund of its fixed deposits together with the accrued interest thereon. I found that the plaintiff had made out its case and granted the reliefs prayed for in terms of prayers (a) and (f) of the statement of claim with the amendments that the accrued interest on the sum of RM15,117,528.50 should be calculated based on the bank's prevailing fixed-deposit interest rates compounded every three months from the dates of deposit until 24 June 1993 and, thereafter, from 25 June 1993, compounded annually at the bank's applicable annual fixed-deposit rate until 23 May 2006 and, thereafter, ie from 24 May 2006, at 8% interest per annum compounded annually until the judgment is satisfied, and that the costs of this action be paid to the plaintiff by the bank on a party-to-party basis after being taxed, unless otherwise agreed upon. I made no order on the other reliefs sought by the plaintiff but granted liberty to the parties to apply on the applicable interest rates after the bank had provided the plaintiff with the same.

[27] At the same time, I dismissed the plaintiff's application in encl. (49) with costs as I was of the view that as the plaintiff had made a business decision to place its monies on fixed deposit in Ringgit Malaysia with the bank in Malaysia, it should not be allowed to convert the monies to Deutsche Marks and Euros with retrospective effect to its advantage. It had to bear the risk that was attendant upon its business decision. As the plaintiff chose to invest in Malaysia, it had to abide by the economic regime in

Malaysia. It would, of course, on realization of the judgment sum be at liberty to convert the same into any currency of its choice at the prevailing rate of conversion to repatriate the monies out of Malaysia.